



Wolters Kluwer
CCH



GLOBAL TAX WEEKLY

a closer look

ISSUE 67 | FEBRUARY 20, 2014

SUBJECTS TRANSFER PRICING INTELLECTUAL PROPERTY VAT, GST AND SALES TAX CORPORATE TAXATION INDIVIDUAL TAXATION REAL ESTATE AND PROPERTY TAXES INTERNATIONAL FISCAL GOVERNANCE BUDGETS COMPLIANCE OFFSHORE

SECTORS MANUFACTURING RETAIL/WHOLESALE INSURANCE BANKS/FINANCIAL INSTITUTIONS RESTAURANTS/FOOD SERVICE CONSTRUCTION AEROSPACE ENERGY AUTOMOTIVE MINING AND MINERALS ENTERTAINMENT AND MEDIA OIL AND GAS

COUNTRIES AND REGIONS EUROPE AUSTRIA BELGIUM BULGARIA CYPRUS CZECH REPUBLIC DENMARK ESTONIA FINLAND FRANCE GERMANY GREECE HUNGARY IRELAND ITALY LATVIA LITHUANIA LUXEMBOURG MALTA NETHERLANDS POLAND PORTUGAL ROMANIA SLOVAKIA SLOVENIA SPAIN SWEDEN SWITZERLAND UNITED KINGDOM EMERGING MARKETS ARGENTINA BRAZIL CHILE CHINA INDIA ISRAEL MEXICO RUSSIA SOUTH AFRICA SOUTH KOREA TAIWAN VIETNAM CENTRAL AND EASTERN EUROPE ARMENIA AZERBAIJAN BOSNIA CROATIA FAROE ISLANDS GEORGIA KAZAKHSTAN MONTENEGRO NORWAY SERBIA TURKEY UKRAINE UZBEKISTAN ASIA-PAC AUSTRALIA BANGLADESH BRUNEI HONG KONG INDONESIA JAPAN MALAYSIA NEW ZEALAND PAKISTAN PHILIPPINES SINGAPORE THAILAND AMERICAS BOLIVIA CANADA COLOMBIA COSTA RICA ECUADOR EL SALVADOR GUATEMALA PANAMA PERU PUERTO RICO URUGUAY UNITED STATES VENEZUELA MIDDLE EAST ALGERIA SAUDI ARABIA BAHRAIN BOTSWANA DUBAI EGYPT ETHIOPIA EQUATORIAL GUINEA IRAQ KUWAIT MOROCCO NIGERIA OMAN QATAR SAUDI ARABIA TUNISIA LOW-TAX JURISDICTIONS ANDORRA ARUBA BAHAMAS BARBADOS BELIZE BERMUDA BRITISH VIRGIN ISLANDS CAYMAN ISLANDS COOK ISLANDS CURACAO GIBRALTAR GUERNSEY ISLE OF MAN JERSEY LABUAN LIECHTENSTEIN MAURITIUS MONACO TURKS AND CAICOS ISLANDS VANUATU



Wolters Kluwer

CCH

GLOBAL TAX WEEKLY

a closer look

Global Tax Weekly – A Closer Look

Using the unrivalled worldwide multi-lingual research capabilities of leading law and tax publisher Wolters Kluwer and its new acquisition BSI (The Lowtax Network), CCH publishes Global Tax Weekly — A Closer Look (GTW) as an indispensable up-to-the-minute guide to today's shifting tax landscape for all tax practitioners and international finance executives.

Topicality, thoroughness and relevance are our watchwords: BSI's network of expert local researchers covers 130 countries and provides input to a US/UK team of editors outputting 100 tax news stories a week. GTW highlights 20 of these stories each week under a series of useful headings, including industry sectors (e.g. manufacturing), subjects (e.g. transfer pricing) and regions (e.g. asia-pacific).

Alongside the news analyses are a wealth of feature articles each week covering key current topics in depth, written by a team of senior international tax and legal experts and supplemented by commentative topical news analyses. Supporting features include a round-up of tax treaty developments, a report on important new judgments, a calendar of upcoming tax conferences, and "The Jester's Column," a light-hearted but merciless commentary on the week's tax events.

Read Global Tax Weekly — A Closer Look in printable PDF form, on your iPad or online through Intelliconnect, and you'll be a step ahead of your world on Monday morning!

CONTENTS

FEATURED ARTICLES

Can The Current Climate Of Hostility Towards The Use Of Hybrid Instruments And Entities In International Tax Planning Be Advantageous For Some?

by Philippos Aristotelous and Stavros Supashis, Andreas Neocleous & Co LLC, Cyprus

5

Global Transfer Pricing Developments: Into The Unknown

by Stuart Gray, Senior Editor, Global Tax Weekly

9

Topical News Briefing: Austria Between The Devil And The Deep Blue Sea

by the Global Tax Weekly Editorial Team

18

HMRC's Approach To Swiss Bank Account Holders

by John Cassidy, partner at Crowe Clark Whitehill, United Kingdom

19

NEWS ROUND-UP

Country Focus: United States

45

Top US House Democrat Joins In TPA Bill Rejection

US Expatriations Reach Record Levels In 2013

Pass-Through Growth Has Implications For US Tax Reform

IRS Ups US Tax Return Filings

IRS Loses Appeal Over Tax Preparer Reforms

Brief Outlines On The Portuguese Corporate Income Tax Reform And Other Investor-Friendly Tax Measures Recently Enacted

by Bruno Santiago and António Queiroz Martins, Morais Leitão, Galvão Teles, Soares da Silva and Associates, Lisbon, Portugal

22

Topical News Briefing: Goodbye Uncle Sam

by the Global Tax Weekly Editorial Team

25

Denmark – A Tax Haven?

by Artur Bugsgang, partner at leading Danish law firm LETT

26

Canada's Economic Action Plan 2014

by Stuart Gray, Senior Editor, Global Tax Weekly

30

Malta: Qualifying Employment In Innovation And Creativity (Personal Tax) Rules

by Justin Spiteri, Mahoney & Co., independent member of Morison International

42

Budgets

51

No New Taxes For Canada, Says Flaherty

Selective Tax Hikes Predicted In South African Budget

French Court Warns Of Fiscal Shortfall In 2014

Australian Industry Group Sets Out Budget Priorities

Switzerland Posts Positive Results For 2013

Shome Backs Lower Indian Tax Rates

Industry Update: Financial Services

Hypo Bank Crisis Ends Tax Cut Hopes, Austrian Institute Says

Austria Rules Out End To Bank Tax

Luxembourg, Austria Hold Savings Tax Talks

EU, Switzerland Set For Fresh Savings Tax Talks

Belgium's Geens Preserves Savings Tax Perk

58

European Union

EU Warns Switzerland: Restrict Migration, Lose Free Trade

Malta Reiterates Opposition To EC's FTT Proposal

MEPs Urge Caution On US Product Talks

EU, WTO Hold Trade Talks

62

TAX TREATY ROUND-UP **65**

CONFERENCE CALENDAR **67**

IN THE COURTS **78**

THE JESTER'S COLUMN **84**

The unacceptable face of tax journalism

Can The Current Climate Of Hostility Towards The Use Of Hybrid Instruments And Entities In International Tax Planning Be Advantageous For Some?

by Philippos Aristotelous and Stavros Supashis, Andreas Neocleous & Co LLC, Cyprus



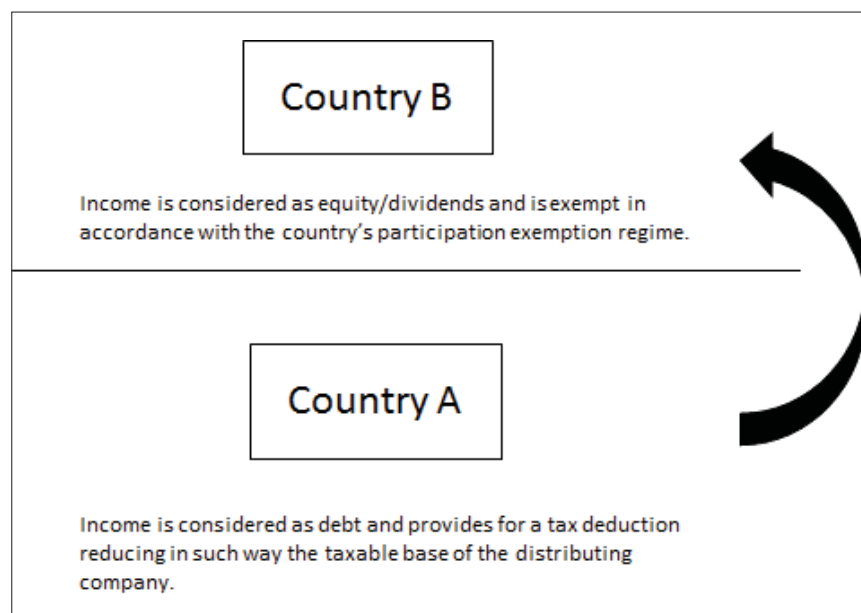
The importance of hybrid instruments in international tax planning has increased dramatically over the past decade and has created tremendous opportunities for both companies and financial services practitioners. Their increasing importance and ability to create substantial tax benefits for taxpayers have attracted the attention of governments worldwide, who view the benefits they create as artificial, and so are seeking to diminish their effectiveness.

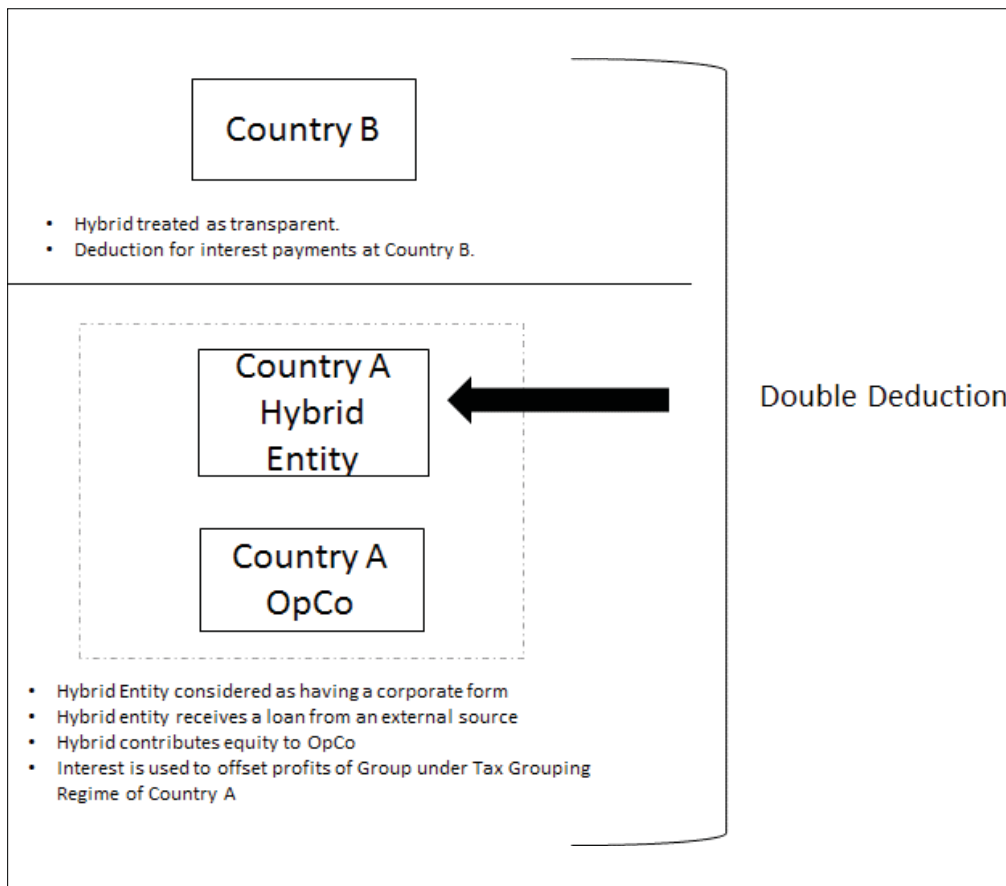
As a first step in analyzing the issue we need to define what is meant by a hybrid instrument or a hybrid entity. In summary it is an instrument or entity, as the case may be, the characteristics of which allow it to arbitrage mismatches arising between various national legislative measures in order for the interested parties to optimize their tax position.

Hybrid instruments are mostly used for financing operations. The interposition of a hybrid instrument can create a double benefit, in the form of a tax deductible interest expense in the country of residence of the payer,

and creation of tax-exempt income in the country of the recipient of the income. This is due to the fact that certain characteristics of the instrument cause it to be treated as a loan by the tax authorities of the country of payment, but to be treated as an equity interest by the authorities in the country in which the income is received, allowing the recipient to take advantage of a domestic participation exemption regime or its equivalent.

Additionally hybrid instruments can be utilized in instances of domestic withholding tax "shopping"





arbitraging the differences, tax-exempt income and taxable deductions can be created.

The extensive use of hybrids in international tax planning and the resultant loss of tax revenues has caused governments to take action, both collectively and unilaterally, to rein in their use. The latest collective initiative is the Organization for Economic Cooperation and Development's ("OECD") Action Plan to counter Base Erosion

and Profit Shifting ("BEPS"), announced in July 2013. In many respects this is a continuation of the Harmful Tax Practices initiative of the 1990s. The OECD has published an action plan and has set ambitious deadlines to achieve its goals. The action plan specifically addresses the issue of hybrid instruments and the measures under consideration include amendment of the OECD Model Tax Convention to deny an exemption of income which has previously caused a deduction at source out of the taxable base of the payor and to deny a deduction if the corresponding income will not be taxable in the hands of the recipient.

as various source countries tend to interpose hybrid instruments in order to avoid withholding taxes on certain items of income by re-characterizing income from, for example, dividends as interest and vice versa.

A hybrid entity is one which is treated as tax-transparent by the legislation of one country and as a corporate vehicle by another. Generally countries do not have a uniform approach as to how to tax foreign entities: some do so on the same basis as domestic entities and others adopt an opt-in opt-out approach which gives the members of the company the ability to choose the way which the foreign entity will be taxed (US check the box system). By

At a European level efforts to counter what the authorities view as over-aggressive tax planning have

increased in recent years, in response to the fall in tax revenues that has resulted from the global financial crisis. The European Commission has announced that it intends to introduce amendments to both the Parent-Subsidiary Directive ("P/S Directive") and the European Union Savings Directive ("EUSD") which will specifically address the issue of hybrid instruments.

In 2012 the European Commission adopted an Action Plan which included more than 30 measures to combat tax fraud and tax evasion. These included a proposal to close loopholes in the P/S Directive. The action plan was substantiated through a proposal to amend the P/S Directive which will deny the benefits of the P/S directive to items of income which had already provided for a deduction at the level of the payor (similar to the recommendations of the OECD).

The EUSD applies to payments of income from EU paying agents (as defined in the EUSD) to individual tax residents in the EU. In general the EUSD requires an exchange of information by member states in relation to the recipient of income. Belgium, Luxembourg and Austria were granted temporary exemption from the requirement to exchange information and were given the option to allow taxpayers to choose between disclosure of interest or payment of a withholding tax, currently at the rate of 35 percent, in place of information exchange. As the definition of interest payments in the EUSD is narrow, it has been relatively easy for paying agents to structure their payments in relation to some

products so as to avoid the payment falling within the definition of "debt claims of every kind." The new amendments seek to extend the definition of interest so as to close these loopholes.

A number of countries have put in place measures to address the issue of hybrid instruments unilaterally through domestic law provisions such as the recently-introduced German anti-hybrid rules (applicable to dividends for fiscal year 2014 onwards) which deny the 95 percent exemption on dividends received by corporate shareholders if the dividend payment was treated as a tax-deductible expense at the level of the foreign distributing entity. Similar rules are also in place in Italy. Anti-hybrid rules can also be found in certain tax treaties such as the rule included in article 4 of the US-Canada treaty which denies treaty benefits to certain income, profit or gains derived through, or paid by, a "hybrid" entity.

It is clear that the authorities have hybrid instruments firmly in their sights and that a large number of current tax structures are likely to lose their usefulness as the trend gathers momentum. This will undoubtedly encourage various jurisdictions to amend their domestic tax legislation so as to achieve similar results.

Most structures involving Cyprus are not affected as its advantageous domestic tax regime does not depend on the use of hybrid instruments or entities. As a result businesses using Cyprus and Cyprus-based structures are not likely to have to take any significant steps towards complying with the

new era of tax planning, as far a hybrid instruments and entities are concerned. Nevertheless, there are still challenges ahead, and Cyprus will need to keep

abreast of international developments in order to maintain and enhance its position on the international tax planning scene.